



COMMODITY FUTURES TRADING COMMISSION

Comparability Determination for the European Union: Dually-Registered

Derivatives Clearing Organizations and Central Counterparties

AGENCY: Commodity Futures Trading Commission.

ACTION: Notice of Comparability Determination for Certain Requirements Under the European Market Infrastructure Regulation.

SUMMARY: The Commodity Futures Trading Commission (the “Commission” or “CFTC”) has determined that certain laws and regulations applicable in the European Union (“EU”) provide a sufficient basis for an affirmative finding of comparability with respect to certain regulatory obligations applicable to derivatives clearing organizations (“DCOs”) that are registered with the Commission and are authorized to operate as central counterparties (“CCPs”) in the EU. The Commission’s determination provides for substituted compliance with respect to requirements for financial resources, risk management, settlement procedures, and default rules and procedures.

DATES: This determination will become effective upon publication in the Federal Register.

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SUPPLEMENTARY INFORMATION:

I. Introduction

On February 10, 2016 Commission Chairman Timothy Massad issued a joint statement with Commissioner Jonathan Hill of the European Commission setting forth a common approach regarding the regulation of CCPs. Under the common approach, the European Commission (“EC”) will propose a third-country equivalence decision (“Equivalence Decision”) regarding the Commission’s regulatory regime for DCOs, which is a prerequisite for the European Securities and Markets Authority (“ESMA”) to recognize U.S. DCOs as equivalent third-country CCPs. Once recognized by ESMA, U.S. DCOs may continue to operate and provide clearing services in the EU.

This Notice is being issued in connection with the resolution of equivalence for U.S. DCOs. For an Equivalence Decision under Article 25 of the European Market Infrastructure Regulation (“EMIR”), one of the conditions requires that the legal and supervisory regime of the United States must include an “effective equivalent system” for the recognition of CCPs authorized in the EU under EMIR.¹ As described below, U.S. law and CFTC regulations require that foreign-based CCPs register with the CFTC in certain circumstances. If registered, they must comply with the relevant U.S. requirements, including the Commission regulations applicable to registered DCOs.

Under this Notice, EU-based CCPs that register with or are currently registered with the Commission as DCOs and that are authorized to operate in the EU may comply

¹ See Regulation (EU) No 648/2012 of the European Parliament and the Council on OTC derivatives, central counterparties and trade repositories of 4 July 2012 (‘EMIR’), Art. 25(6).

with certain Commission requirements for financial resources, risk management, settlement procedures, and default rules and procedures (as set forth in this Notice) by complying with the terms of corresponding requirements under the EMIR Framework, as defined below.

II. Statutory and Regulatory Framework for Registration of non-U.S. CCPs

The Commodity Exchange Act (“CEA”) does not impose geographic limitations on the registration of DCOs. Nor does it mandate that clearing of futures traded on U.S. exchanges must take place in the United States.² To the contrary, it permits futures traded on exchanges in the United States to be cleared outside the United States. However, the CEA and CFTC regulations require that foreign-based CCPs that wish to clear such futures be registered with the Commission and comply with CFTC regulations.³ In addition, consistent with Section 2(i) of the CEA, foreign-based CCPs that clear swaps with a sufficient nexus to U.S. commerce must register with the Commission.⁴

Thus, under this regulatory framework, a number of foreign-based CCPs have been registered with the Commission for some time. LCH.Clearnet Ltd., which is based in London, for example, has been registered with the Commission since 2001, and thus has been subject to dual supervision by UK authorities and the Commission since long before the EU adopted its current regulatory scheme – EMIR.⁵ This dual registration

² 7 U.S.C. 7a-1(a).

³ See generally 7 U.S.C. 7(d)(9)(iii) and (11); 17 CFR 38.601.

⁴ 7 U.S.C. 7a-1(a); 17 CFR 39.3; see also 7 U.S.C. 2(i) (providing that the CEA’s swap-related provisions shall not apply to activities outside the United States unless those activities have a direct and significant connection with activities in, or effect on, commerce of the United States or contravene such rules or regulations as the Commission may prescribe or promulgate as are necessary or appropriate to prevent the evasion of any provision of the CEA).

⁵ Regulation (EU) No 648/2012 on OTC derivatives, central counterparties and trade repositories.

system has been a foundation on which the cleared swaps market grew to be a global market. In addition to LCH.Clearnet Ltd., there are currently five other foreign-based DCOs that are registered both with the Commission and their home country regulators: Singapore Exchange Derivatives Clearing Limited (home country regulator is the Monetary Authority of Singapore), LCH.Clearnet SA (home country regulators are the Autorité de contrôle prudentiel et résolution, the Autorité des marchés financiers, and the Banque de France), ICE Clear Europe Ltd. (home country regulator is Bank of England), Natural Gas Exchange (home country regulator is the Alberta Securities Commission), and Eurex Clearing AG (home country regulators are Bundesanstalt für Finanzdienstleistungsaufsicht (BaFin) and Deutsche Bundesbank). Two additional foreign-based CCPs have applications pending before the Commission for registration as DCOs (CME Clearing Europe Ltd. and Japan Securities Clearing Corporation). Additionally, the Commission has provided exemptions from registration for foreign-based CCPs that clear proprietary swaps positions for their U.S. members and affiliates but not for U.S. customers generally. (These foreign-based DCOs also do not clear futures traded on U.S. designated contract markets (“DCMs”).) These exemptions have been issued pursuant to Section 5b(h) of the CEA, which permits the Commission to exempt a clearing organization from DCO registration for the clearing of swaps to the extent that the Commission determines that such clearing organization is subject to comparable, comprehensive supervision by appropriate government authorities in the clearing organization’s home country.⁶

⁶ 7 U.S.C. 7a-1(h).

For purposes of the granting of exemptions to foreign-based CCPs that are not clearing futures traded on U.S. DCMs nor clearing swaps for U.S. customers, the Commission has determined that a supervisory and regulatory framework that is consistent with the Principles for Financial Market Infrastructures (“PFMIs”) can be considered to be comparable to and as comprehensive as the supervisory and regulatory framework established by the CEA and part 39 of the Commission’s regulations.⁷

Pursuant to this authority, the Commission has granted exemptions to clearing organizations in Australia, Japan, South Korea, and Hong Kong, provided that each exempt CCP not offer customer clearing services for U.S. persons and limit direct clearing by U.S. persons and futures commission merchants (“FCMs”) to the following circumstances: (1) “A U.S. person that is a clearing member of [the exempt CCP] may clear swaps for itself and those persons identified in the Commission’s definition of ‘proprietary account’ set forth in Regulation 1.3(y)”; (2) “A non-U.S. person that is a clearing member of [the exempt CCP] may clear swaps for any affiliated U.S. person identified in the definition of ‘proprietary account’ set forth in Regulation 1.3(y)”; and (3) “An entity that is registered with the Commission as an FCM may be a clearing member of [the exempt CCP], or otherwise maintain an account with an affiliated broker that is a clearing member, for the purpose of clearing swaps for itself and those persons identified in the definition of ‘proprietary account’ set forth in Regulation 1.3(y).”⁸

⁷ The PFMIIs were jointly issued by the Committee on Payment and Settlement Systems (now, the Committee on Payments and Market Infrastructures (“CPMI”)) of the Bank for International Settlements and the Technical Committee of the International Organization of Securities Commissions (“IOSCO”) in April 2012. The PFMIIs are available at <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD377.pdf>.

⁸ See *In re* Petition of ASX Clear (Futures) Pty Limited for Exemption from Registration as a Derivatives Clearing Organization (Aug. 18, 2015); *In re* Petition of Japan Securities Clearing Corp. for Exemption from Registration as a Derivatives Clearing Organization (Oct. 26, 2015); *In re* Petition of Korea Exchange, Inc. for Exemption from Registration as a Derivatives Clearing Organization (Oct. 26, 2015); *In*

To clear U.S. customer transactions, the Commission requires that a CCP register with the Commission as a DCO and such a DCO becomes subject to Section 4d of the CEA, which establishes a customer protection regime for futures, options, and swaps customers.⁹ For example, with respect to swaps customers, Section 4d(f)(1) states that it shall be unlawful for any person to accept money, securities, or property (funds) from a swaps customer to margin a swap cleared through a DCO unless the person is registered as an FCM.¹⁰ Additionally, Section 4d(f)(2) requires segregation of cleared swaps customer funds from the funds of the FCM, and Section 4d(f)(6) extends these segregation requirements to DCOs.¹¹ These provisions of the CEA interlock with the commodity broker provisions of the Bankruptcy Code, Subchapter IV of Chapter 7.¹² No EU-based CCP has sought an exemption from registration. This is because EU-based CCPs offer, or are seeking to offer, clearing for U.S. customers and thus have obtained or are seeking to obtain, registration as DCOs. Nevertheless, EU-based CCPs that do not clear swaps for U.S. customers may petition the Commission for exempt DCO status.

Additionally, in all instances in which the Commission has granted registration to a foreign-based CCP, it also has entered into a memorandum of understanding or similar arrangement (“MOU”) with the CCP’s home country regulator(s). Such MOUs establish

re Petition of OTC Clearing Hong Kong Ltd. for Exemption from Registration as a Derivatives Clearing Organization (Dec. 21, 2015).

⁹ 7 U.S.C. 6d(a), (b), and (f).

¹⁰ Section 4d(f)(1) of the CEA, 7 U.S.C 6d(f)(1), states, in relevant part, that it shall be unlawful for any person to accept any money, securities, or property (or to extend any credit in lieu of money, securities, or property) from, for, or on behalf of a swaps customer to margin, guarantee, or secure a swap cleared by or through a derivatives clearing organization (including money, securities, or property accruing to the customer as the result of such a swap), unless the person shall have registered under the CEA with the Commission as a futures commission merchant, and the registration shall not have expired nor been suspended nor revoked.

¹¹ 7 U.S.C 6d(f)(2) and (6).

¹² See 11 U.S.C. 761-767; see also Section 101(6) of the Bankruptcy Code, 11 U.S.C. 101(6).

a framework pursuant to which the Commission and the CCP's home country regulator(s) intend to cooperate with each other in fulfilling their respective regulatory responsibilities with respect to covered cross-border entities, including CCPs licensed by the home country regulator(s) and registered with the Commission. Specifically, such an MOU sets forth procedures for, among other things, information sharing between the CFTC and the home country regulator(s), notification of certain material information, conduct of on-site visits, and the use and treatment of non-public information.

III. Regulation of CCPs in the EU

EU-based CCPs are subject to the regulations laid down in EMIR and the Regulatory Technical Standards ("RTS") (collectively, the "EMIR Framework").¹³ EMIR and the RTS establish uniform legal requirements for EU CCPs that, as EU-level legislation, have an immediate, binding, and direct effect in all EU member states without the need for additional action by national authorities.¹⁴ Moreover, where the European Parliament and the European Council have passed EU-level legislation, EU member states cannot legislate laws that duplicate or conflict with EMIR.¹⁵

The European Parliament and the European Council passed EMIR on July 4, 2012, which entered into force on August 16, 2012. The relevant technical standards for CCPs, including the RTS for capital requirements ("RTS-CR") and the RTS for central counterparties ("RTS-CCP"), generally entered into force on March 15, 2013.

¹³ For the purposes of this Notice the Commission only considered those EMIR Framework provisions published as of the date of this Notice. The relevant RTS include: Commission Delegated Regulation No. 152/2013 with regard to regulatory technical standards on capital requirements for central counterparties ("RTS-CR"); and Commission Delegated Regulation No. 153/2013 with regard to regulatory technical standards on requirements for central counterparties ("RTS-CCP").

¹⁴ See EMIR (stating that "[t]his Regulation shall be binding in its entirety and directly applicable in all Member States.").

¹⁵ EMIR Article 13(1).

Pursuant to EMIR, each EU member state is responsible for implementing the EMIR Framework by designating a national competent authority(s) (“NCA”) to authorize and supervise the day-to-day operations of CCPs established in its territory. The NCAs are required to regularly review how the CCP complies with EMIR by examining the CCP’s rules, arrangements, procedures, and mechanisms, and to evaluate the risks to which such CCPs are, or might be, exposed. At a minimum, these reviews and examinations must occur at least annually. As part of such reviews and evaluations, the CCP is subject to on-site inspections.¹⁶

Additionally, for each authorized CCP, a college of supervisors is established that comprises members of the NCA, ESMA, other EU national authorities that may supervise entities on which the operations of that CCP might have an impact (i.e., selected clearing members, trading venues, interoperable CCPs and central securities depositories), as well as members of the European System of Central Banks (ESCB), as relevant.¹⁷ The NCAs regularly, and at least annually, inform the college of the results of the review and evaluation of the CCP, including any remedial action taken or penalty imposed.¹⁸ The CCP college is responsible for reaching an opinion on (1) the authorization of a CCP; (2) extensions of authorization; and (3) any changes to a CCP’s risk model.

While NCAs remain in charge of supervising CCPs, ESMA, as an independent European supervisory authority, validates changes to the risk models of authorized CCPs and is responsible for harmonizing and coordinating the implementation of EMIR across the EU member states. ESMA is managed by a Board of Supervisors, which is composed

¹⁶ See EMIR Articles 21 and 22.

¹⁷ Id. at Article 18.

¹⁸ Id. at Articles 12 and 21

of the heads of 28 national authorities (where there is more than one national authority in a Member State those authorities agree which of their heads will represent them), with observers from Norway, Iceland, and Liechtenstein. The Board makes decisions on the compliance by NCAs with community legislation, interpretation of community legislation, decisions in crisis situations, the approval of draft technical standards, guidelines, peer reviews, and any reports that are developed.¹⁹

IV. Comparable and Comprehensive Standard

Consistent with CEA Section 2(i) and principles of international comity, in the case of foreign-based DCOs, the Commission will make a comparability determination on a requirement-by-requirement basis, rather than on the basis of the foreign regime as a whole.²⁰ In making its comparability determinations, the Commission may include conditions that address, among other things, timing and other issues related to coordinating the implementation of reform efforts across jurisdictions.

In evaluating whether a particular category of foreign regulatory requirement(s) is comparable and comprehensive to the corollary requirement(s) under the CEA and Commission regulations, the Commission will take into consideration all relevant factors, including, but not limited to: the comprehensiveness of the requirement(s); the scope and objectives of the relevant requirement(s); the comprehensiveness of the foreign

¹⁹ See ESMA: Board of Supervisors and NCAs, <https://www.esma.europa.eu/about-esma/governance/board-supervisors-and-ncas>.

²⁰ The Commission has taken analogous action with respect to foreign-based swap dealers and major swap participants. Cf. 78 FR 78864 (Dec. 27, 2013) (Australia); 78 FR 78852 (Dec. 27, 2013) (Hong Kong); 78 FR 78910 (Dec. 27, 2013) (Japan – Entity Level Requirements); 78 FR 78890 (Dec. 27, 2013) (Japan – Transaction Level Requirements); 78 FR 78899 (Dec. 27, 2013) (Switzerland); 78 FR 78839 (Dec. 27, 2013) (Canada); 78 FR 78923 (Dec. 27, 2013) (EU – Entity Level Requirements); 78 FR 78878 (Dec. 27, 2013) (EU – Transaction Level Requirements); see also 78 FR 45292 (July 26, 2013).

regulator's supervisory compliance program; and the foreign jurisdiction's authority to support and enforce its oversight of the registrant.

In making this comparability determination, the Commission is relying on the provisions of the EMIR Framework. The Commission assumes that the provisions of the EMIR Framework discussed herein are in full force and effect and that the description of the EMIR Framework that is contained within this Notice is accurate and complete.²¹ The Commission also assumes that the provisions of the EMIR Framework discussed herein have been implemented in accordance with their terms and there are no Member State or EU laws, regulations, or actions of the NCAs or any other authorities that are contrary to the provisions of the EMIR Framework. Further, the Commission's determination is based on the EMIR Framework as it exists at this time; any changes to the EMIR Framework (including, but not limited to, changes in the relevant supervisory or regulatory regime) could, depending on the nature of the change, invalidate the Commission's comparability determination.

V. Comparability Determination

The following section presents the requirements imposed by specific sections of the CEA and Commission regulations applicable to DCOs that are the subject of this comparability determination. Following the discussion of each Commission requirement, the Commission provides the corresponding provision of the EMIR Framework.

The Commission's determinations in this regard are intended to inform the public of the Commission's views regarding whether the specific provisions of the EMIR

²¹ The Commission additionally provided the EC and ESMA the opportunity to consult regarding the relevant provisions of the EMIR Framework described in this Notice; however, in reaching its conclusions the Commission ultimately relied upon the English-language published text of the provisions of the EMIR Framework.

Framework may be comparable to, and as comprehensive as, specific requirements in the CEA and CFTC regulations and, therefore, may form the basis for substituted compliance. The descriptions provided herein of CEA and CFTC requirements, as well as the provisions of the EMIR Framework, are summaries of the actual provisions and are qualified by reference to them. Statements of regulatory objectives are general in nature and provided only for the purpose of this Notice. Likewise, the Commission's summary of what is comparable as between specific CEA and CFTC requirements on the one hand and corresponding provisions of the EMIR Framework on the other is only a summary. In particular, there may be aspects that are not cited, including particular features that may not be comparable, but that do not affect the overall determination with respect to that provision or set of provisions.

A. Financial Resources (Regulation 39.11)

CEA Section 7a-1(c)(2)(B) ("Core Principle B") establishes general requirements for DCOs to have adequate financial resources. To implement Core Principle B the Commission adopted regulation 39.11, which requires a DCO to maintain financial resources sufficient to cover its exposures with a high degree of confidence and to enable it to perform its functions in compliance with the core principles set out in Section 5b of the CEA.

Commission Requirement: Regulation 39.11 sets forth requirements by which a DCO must identify and adequately manage its general business risks and hold sufficient liquid resources to cover potential losses that are not related to clearing members' defaults so that the DCO can continue to provide services as a going concern.

Regulation 39.11 provides that a DCO's financial resources will be considered sufficient if their value, at a minimum, exceeds the total amount that would enable the DCO to meet its financial obligations to its clearing members notwithstanding a default by the clearing member creating the largest financial exposure for the DCO in extreme but plausible market conditions ("Cover 1").²² A DCO may use the following types of financial resources to satisfy this requirement, including: the DCO's own capital; guaranty fund deposits; default insurance; potential assessments for additional guaranty fund contributions, if permitted by the DCO's rules; and any other financial resource deemed acceptable.²³

On a monthly basis, a DCO must perform stress testing that will allow it to make a reasonable calculation of the financial resources needed to meet its Cover 1 requirement. A DCO has reasonable discretion to determine the methodology it uses to compute its Cover 1 requirement; however, the Commission may review the methodology and require changes as appropriate.²⁴ A DCO may allocate a financial resource to satisfy its Cover 1 credit risk or its operating costs, but it may not allocate a financial resource to satisfy both its Cover 1 credit risk and its operating costs.²⁵

If a DCO's rules provide for assessments for additional guaranty fund contributions, then the DCO must: have rules requiring that its clearing members have the ability to meet an assessment within the time frame of a normal end-of-day variation settlement cycle; monitor the financial and operational capacity of its clearing members to meet potential assessment(s); apply a 30% haircut to the value of potential

²² 17 CFR 39.11(a)(1).

²³ 17 CFR 39.11(b)(1).

²⁴ 17 CFR 39.11(c)(1).

²⁵ 17 CFR 39.11(b)(3).

assessments; and only count the value of assessments after the haircut, to meet up to 20% of those obligations.²⁶

In addition, CFTC regulation 39.11 provides that a DCO must effectively measure, monitor, and manage its liquidity risks, maintaining sufficient liquid resources such that it can, at a minimum, fulfill its cash obligations when due.²⁷ A DCO also must hold its assets in a manner that minimizes the risk of loss or delay in accessing them.²⁸ The financial resources the DCO allocates to meet this liquidity requirement must be sufficiently liquid to enable the DCO to fulfill its obligations as a CCP during a one-day settlement cycle.²⁹ A DCO must maintain cash, U.S. Treasury obligations, or high quality, liquid, general obligations of a sovereign nation, in an amount equal or greater than an amount calculated as follows:

- Calculate the average daily settlement pay for each clearing member over the last fiscal quarter;
- Calculate the sum of those average daily settlement pays; and
- Using that sum, calculate the average of its clearing members' average pays.³⁰

A DCO may take into account a committed line of credit or similar facility for the purposes of meeting the remainder of this liquidity requirement.

CFTC regulation 39.11 further provides that the assets a DCO holds in a guaranty fund must have minimal credit, market, and liquidity risks and must be readily accessible

²⁶ 17 CFR 39.11(d)(2).

²⁷ 17 CFR 39.11(e)(1)(i).

²⁸ Id.

²⁹ 17 CFR 39.11(e)(1)(ii).

³⁰ 17 CFR 39.11(e)(1)(ii).

on a same-day basis.³¹ Additionally, letters of credit are not permissible assets for a guaranty fund.³²

Finally, CFTC regulation 39.11 provides that a DCO's cash balances must be invested or placed in safekeeping in a manner that bears little or no principal risk.³³

Regulatory Objective: Core Principle B and the Commission's implementing regulations are designed to establish uniform standards that further the goals of avoiding market disruptions and financial losses to market participants and the general public, and avoiding systemic problems that could arise from a DCO's failure to maintain adequate resources. The regulations promote financial strength and stability, thereby fostering efficiency and a greater ability to compete in the broader financial market.

As highlighted by the events of 2007-2008 in global financial markets, maintaining sufficient financial resources is a critical aspect of any financial entity's risk management system, and ultimately contributes to the goal of stability in the broader financial markets. By setting specific standards with respect to how DCOs must access and monitor the adequacy of their financial resources, Core Principle B and the Commission's implementing regulations contribute to a DCO's maintenance of sound risk management practices and further the goal of minimizing systemic risk.

Comparable EU Law and Regulations: The following provisions of the EMIR Framework address financial resources.

EMIR, Art. 43: At all times, a CCP shall maintain sufficient prefunded available financial resources to enable the CCP to withstand the default of at least the two clearing

³¹ 17 CFR 39.11(e)(3)(i).

³² 17 CFR 39.11(e)(3)(iii).

³³ 17 CFR 39.11(e)(3)(ii).

members to which it has the largest exposure under extreme but plausible market conditions. Such prefunded financial resources shall include dedicated resources of the CCP, shall be freely available to the CCP, and shall not be used to meet the CCP's capital requirements.

RTS-CCP, Art. 51(2) and 53(1): On a regular basis, a CCP shall conduct stress tests designed to ensure that its combination of margin, default fund contributions, and other financial resources are sufficient to cover the default of at least the two clearing members to which the CCP has the largest exposures under extreme but plausible market conditions. As part of its stress testing, the CCP also shall examine potential losses resulting from the default of entities in the same corporate group as the two clearing members to which it has the largest exposure under extreme but plausible market conditions.

RTS-CCP, Art. 30(2) and 59(5): A CCP shall develop a framework for defining the types of extreme but plausible market conditions based on a range of (1) historical scenarios that could expose it to the greatest risk; and (2) potential future scenarios founded on consistent assumptions regarding market volatility and price correlation across markets and financial instruments, drawing on both quantitative and qualitative assessments of potential market conditions. If a CCP decides that recurrence of a historical instance of large price movements is not plausible, the CCP shall justify to the competent authority its omission from the framework. A CCP shall analyze and monitor its financial resources coverage in the event of defaults by conducting at least daily stress testing using standard and predetermined parameters and assumptions.

EMIR, Art. 44 and 47(3)-(5): At all times, a CCP shall have access to adequate liquidity to perform its services and activities and, on a daily basis, shall measure its potential liquidity needs. Financial instruments posted as margin or as default fund contributions shall be deposited in a manner that ensures the full protection of those financial instruments. Cash deposits of a CCP, other than with a central bank, shall be executed through highly secure arrangements with authorized financial institutions. Where a CCP deposits assets with a third party, it shall ensure that the assets are identifiable separately by means of differently titled accounts.

RTS-CCP, Chapter VIII (Art. 32-34): A CCP shall establish a robust liquidity risk management framework, which shall include, among other things, effective operational and analytical tools to identify, measure, and monitor its settlement and funding flows on an ongoing and timely basis and assess its potential future liquidity needs under a wide range of potential stress scenarios. A CCP shall maintain, in each relevant currency, liquid resources commensurate with its liquidity requirements. These liquid resources shall be limited to the following: cash deposited at a central bank of issue; cash deposited at authorized credit institutions; committed lines of credit; committed repurchase agreements; and/or highly marketable financial instruments that are readily available and convertible into cash on a same-day basis using prearranged and highly reliable funding arrangements.

EMIR, Art. 46 and 47: A CCP shall accept highly liquid collateral with minimal credit and market risk to cover its initial and ongoing exposure to its clearing members and it shall invest its financial resources only in cash or highly liquid financial instruments with minimal market and credit risk.

EMIR, Art. 16 and 47(2): A CCP's capital, including retained earnings and reserves, shall be proportionate to the risk stemming from the activities of the CCP. Capital not invested in cash or highly liquid financial instruments with minimal credit risk, however, shall not count for purposes of calculating a CCP's regulatory capital.

RTS-CR, Art. 2(2): A CCP shall calculate and retain the amount of capital it requires to wind down or restructure. This estimated time span shall be sufficient to ensure an orderly winding down or restructuring of its activities, reorganizing its operations, liquidating its clearing portfolio, or transferring its clearing activities to another CCP, including in stressed market conditions. For the purposes of this RTS, the prescribed time span for purposes of determining sufficient capital to wind down or restructure a CCP's activities is subject to a minimum of six months.

RTS-CCP, Art. 43-46 and Annex II: A debt instrument can be considered highly liquid, bearing minimal credit and market risk if it is issued by or explicitly guaranteed by a government, central bank, multilateral development bank, or the European Financial Stability Facility or the European Stability Mechanism; the CCP can demonstrate that the debt instrument has low credit and market risk based upon an internal assessment; the average time-to-maturity of the CCP's portfolio does not exceed two years; the debt instrument is denominated in a currency the risks of which the CCP can demonstrate it is able to manage or in a currency in which the CCP clears transactions; the debt instrument is freely transferrable and without any regulatory constraint or third party claims that impair liquidation; the debt instrument has an active outright sale or repurchase market with a diverse group of buyers and sellers, including during stress conditions; and reliable price data on the debt instrument is published on a regular basis.

Commission Determination: The Commission finds that the provisions of the EMIR Framework with respect to financial resources are generally similar to the applicable provisions of CFTC Regulation 39.11, and set specific and uniform standards with respect to how CCPs should access and monitor the adequacy of their financial resources. These standards seek to ensure that CCPs can meet their financial obligations to market participants, thus contributing to the financial integrity of the derivatives market as a whole. Both regimes require prefunding of financial resources sufficient to at least cover a default caused by a clearing member creating the largest financial exposure for the EU-based CCP that is dually registered with the CFTC as a DCO (“DCO/CCP”) in extreme but plausible market conditions. Both regimes also require that a DCO/CCP’s financial resources include dedicated resources (e.g., prefunded mutualized resources) and require frequent and regular stress testing of financial resources. Likewise, both regimes require that assets in the default fund have minimal credit, market, and liquidity risks, and be readily accessible on a same-day basis. Additionally, both regimes prohibit a DCO/CCP from allocating the same financial resources to different categories of financial exposure and both regimes require that cash balances must be either invested or appropriately safeguarded in a manner which bears little to no principal risk.

Accordingly, the Commission finds that the provisions of the EMIR Framework with respect to financial resources discussed above and identified below in Table 1(a) are comparable to and as comprehensive as the financial resource requirements of CFTC regulation 39.11, with the exception of 39.11(f), which requires DCOs to submit to the Commission quarterly financial resource reports that include a quarterly financial statement. The Commission recognizes that European CCPs would not have financial

statements prepared in accordance with U.S. Generally Accepted Accounting Principles (“GAAP”) absent Commission registration. Thus, the Commission will permit CCPs to submit financial statements prepared in accordance with International Financial Reporting Standards (“IFRS”), with periodic reconciliation to assist staff in reviewing the financial statements.

Table 1(a): Financial Resources		
Subject Area	CFTC Regulations	EMIR Framework
Default financial resources (Credit risk: Cover 1)	17 CFR 39.11(a)(1) 17 CFR 39.11(b)(1) 17 CFR 39.11(d)(2)	EMIR, Art 43; RTS-CCP, Art 53(1)
Monthly stress-testing of default financial resources	17 CFR 39.11(c)(1)	RTS-CCP, Art. 51(2) and 53(1); RTS-CCP, Art 30(2) and 59(5)
Liquidity of default financial resources	17 CFR 39.11(e)(1)	EMIR, Art 44 and 47(3)-(5); RTS-CCP, Chapter VIII (Art 32-34)
Default fund collateral	17 CFR 39.11(e)(3)(i) 17 CFR 39.11(e)(3)(iii)	EMIR, Art 46 and 47
General business risks (Allocation of financial resources)	17 CFR 39.11(b)(3)	EMIR Art 16 and 47(2); RTS-Capital Requirements for CCP, Art 2(2)
Cash management	17 CFR 39.11(e)(3)(ii)	EMIR, Art 47; RTS-CCP, Art 43-46 and Annex II

B. Risk Management (Regulation 39.13)

CEA Section 7a-1(c)(2)(D) (“Core Principle D”) establishes general requirements for DCOs to have the ability to manage the risks associated with discharging the responsibilities of the DCO through the appropriate tools and procedures. To implement Core Principle D, the Commission adopted regulation 39.13, which requires a DCO to maintain appropriate tools and procedures to manage the risks associated with

discharging the responsibilities of a DCO in compliance with the core principles set out in Section 5b of the CEA.

Commission Requirement: CFTC regulation 39.13 generally requires a DCO to measure its credit exposure to each clearing member not less than once during each business day and to monitor such exposure periodically during the business day. CFTC regulation 39.13 also requires a DCO to limit its exposure to potential losses from defaults by clearing members, through margin requirements and other risk control mechanisms, to ensure that its operations would not be disrupted and that non-defaulting clearing members would not be exposed to losses that non-defaulting clearing members cannot anticipate or control. Finally, CFTC regulation 39.13 also requires that a DCO collect margin from each clearing member sufficient to cover potential exposures in normal market conditions and that each model and parameter used in setting such margin requirements be risk-based and reviewed on a regular basis.

CFTC regulation 39.13 requires a DCO to establish, maintain, and regularly update a written risk management framework (approved by its board of directors) that, at a minimum, clearly identifies and documents the range of risks to which the DCO is exposed, addresses monitoring and managing those risks, and provides a mechanism for internal audit.³⁴

CFTC regulation 39.13 also requires a DCO to appoint a chief risk officer (“CRO”), who must be responsible for implementing the DCO’s written risk management framework and for making appropriate recommendations to the DCO’s risk management

³⁴ 17 CFR 39.13(b).

committee or board of directors.³⁵ Given the importance of the risk management function and the comprehensive nature of the responsibilities of a DCO's chief compliance officer ("CCO"), the Commission previously has stated that it expects that a DCO's CRO and CCO would be two different individuals.³⁶

Pursuant to CFTC regulation 39.13, through margin requirements and other risk control mechanisms, a DCO must limit its exposure to potential losses from defaults by its clearing members to ensure that its operations would not be disrupted and non-defaulting clearing members would not be exposed to losses that they cannot anticipate or control.³⁷

CFTC regulation 39.13 also provides that a DCO must establish initial margin requirements that are commensurate with the risk of each product and portfolio, including any unusual characteristics of, or risks associated with, particular products or portfolios, including but not limited to jump-to-default risk or other similar risk.³⁸ Each model and parameter used in setting initial margin requirements must be risk-based and reviewed on a regular basis.³⁹ On a daily basis, a DCO must determine the adequacy of its initial margin requirements.⁴⁰

The actual coverage of a DCO's initial margin requirements must meet an established confidence level of at least 99%, based on data from an appropriate historical time period, for each product for which the DCO uses a product-based margin methodology; for each spread within or between products for which there is a defined

³⁵ 17 CFR 39.13(c).

³⁶ 76 FR 69363.

³⁷ 17 CFR 39.13(f).

³⁸ 17 CFR 39.13(g)(2)(i).

³⁹ 17 CFR 39.13(g)(1).

⁴⁰ 17 CFR 39.13(g)(6).

spread margin rate; for each account held by a clearing member at the DCO, by house origin and by each customer origin; and for each swap portfolio, including any portfolio containing futures and/or options and held in a commingled account pursuant to CFTC regulation 39.15(b)(2), by beneficial owner.⁴¹ A DCO must determine the appropriate historic time period based on the characteristics, including volatility patterns, of each product, spread, account, or portfolio.⁴²

In addition, CFTC regulation 39.13 provides that on a regular basis, a qualified and independent party must review and validate a DCO's systems for generating initial margin requirements, including its theoretical models, and that this party must not be the person responsible for development or operation of the systems and models being tested.⁴³

A DCO may reduce initial margin requirements for related positions if the price risks with respect to such positions are significantly and reliably correlated – i.e., there is a theoretical basis for the correlation in addition to an exhibited statistical correlation.⁴⁴

Additionally, CFTC regulation 39.13 provides that a DCO must back test its initial margin requirements by comparing its initial margin requirements with historical price changes to determine the extent of actual margin coverage using an appropriate time period but not less than the previous 30 days, as follows: on a daily basis, the DCO must back test products or swaps portfolios that are experiencing significant market

⁴¹ 17 CFR 39.13(g)(2)(iii).

⁴² 17 CFR 39.13(g)(2)(iv).

⁴³ 17 CFR 39.13(g)(3).

⁴⁴ 17 CFR 39.13(g)(4).

volatility; and on at least a monthly basis, the DCO must back test the adequacy of all of its initial margin requirements.⁴⁵

On a daily basis, a DCO must use prudent valuation practices to value assets posted as initial margin.⁴⁶ In particular, a DCO must appropriately reduce its valuation of the assets that it accepts in satisfaction of its initial margin requirements, to reflect credit, market, and liquidity risks, taking into account stressed market conditions, and must evaluate the appropriateness of such haircuts on at least a quarterly basis.⁴⁷

Regulatory Objective: Core Principle D and the Commission's implementing regulations are designed to ensure that each DCO possesses the ability and necessary tools to manage the risks associated with discharging the responsibilities of being a DCO. The Commission's regulation requiring a DCO to maintain and update a written risk management framework seeks to ensure that a DCO carefully has considered its risk management framework, and it will provide guidance to DCO management, staff, and market participants. By requiring a 99% confidence level for initial margin, the Commission's regulations seek to prevent DCOs from competing with respect to how much risk they are willing to take on or from misjudging the amount of risk they would take on if they operated under lower standards. Through requiring independent validation of the DCO's margin models, the Commission's regulations seek to prevent bias in validating the DCO's models. By requiring daily review and back testing, the regulations seek to ensure that DCOs monitor the adequacy of their initial margin requirements.

⁴⁵ 17 CFR 39.13(g)(7).

⁴⁶ 17 CFR 39.13(g)(11).

⁴⁷ 17 CFR 39.13(g)(12).

Comparable EU Law and Regulations: The following provisions of the EMIR Framework address risk management.

RTS-CCP Art. 4: A CCP shall have a sound, written framework for the comprehensive management of all material risks to which it is or may be exposed. In developing its risk management framework, a CCP shall take an integrated and comprehensive view of all relevant risks.

RTS-CCP, Art. 3(3) and 4(6): A CCP shall have a CRO, who shall implement the risk management framework. The CCP shall ensure that the functions of the CRO, CCO, and chief technology officer are carried out by different individuals, who shall be employees of the CCP entrusted with the exclusive responsibility of performing these functions.

EMIR, Art. 48(2): A CCP shall take prompt action to contain losses and liquidity pressures resulting from defaults and shall ensure that the closing out of any clearing member's positions does not disrupt its operations or expose non-defaulting clearing members to losses that they cannot anticipate or control.

EMIR, Art. 41(2), 49(1): A CCP shall adopt models and parameters for setting margin requirements that capture the risk characteristics of the products and swaps cleared and take into account the interval between margin collections, market liquidity, and the possibility of changes over the duration of the transaction. The models shall be validated by the competent authority. A CCP regularly shall review its models and parameters for setting margin requirements and shall subject the models to rigorous and frequent stress tests. A CCP also shall obtain independent validations of its models and parameters.

RTS-CCP, Art. 24(2)(b): In determining the adequate confidence interval for each class of product that it clears, a CCP shall consider, among other factors, the risk characteristics of the class of product, which can include, but are not limited to, volatility, duration, liquidity, non-linear price characteristics, jump-to-default risk and wrong-way risk.

RTS-CCP, Art. 24(1): A CCP shall calculate the initial margins to cover the exposures arising from market movements for each financial instrument that is collateralized on a product basis, over an appropriate time horizon for the liquidation of the position, with a confidence level of 99.5% for over-the-counter derivatives and 99% for all other products.

RTS-CCP, Art. CCP 25: A CCP shall ensure that its model methodology and its validation process for determining initial margin covers at least the latest 12 months and captures a full range of market conditions, including periods of stress.

RTS-CCP, Art 47 and 59(1): At least annually, a CCP shall conduct a comprehensive and well-documented validation of its models, their methodologies, and the liquidity risk management framework used to quantify, aggregate, and manage the CCP's risks.

RTS-CCP, Art. 27 and 59(9): A CCP may allow offsets or reductions in the required margin across the products and swaps that it clears if the price risk of one financial instrument or a set of products or swaps is significantly and reliably correlated, or based on an equivalent statistical parameter of dependence, with the price risk of other products or swaps. The CCP shall demonstrate the existence of an economic rationale for the price correlation. At least annually, a CCP shall test offsets among products and

swaps and how correlations perform during periods of actual and hypothetical severe market conditions.

RTS-CCP, Art. 49 and 60(2): On a daily basis, a CCP shall assess its margin coverage by back testing its margin coverage against expected outcomes derived from the use of margin models to evaluate whether there are any testing exceptions to margin coverage. In conducting such back testing, the CCP shall evaluate its current positions and clearing members, and take into account possible effects from portfolio margining and, where appropriate, interoperable CCPs. The historical time horizons used for back tests shall include data from at minimum the most recent year or as long as a CCP has been clearing the relevant product or swap if that is less than a year.

RTS-CCP, Art. 40(2): A CCP shall mark-to-market its collateral on a near to real-time basis, and where not possible, a CCP shall be able to demonstrate to the competent authorities that it is able to manage the risks.

EMIR, Art. 46(1); RTS-CCP, Art. 41(2) and 59(10): A CCP shall accept highly liquid collateral with minimal credit and market risk to cover its initial and ongoing exposure to its clearing members. It shall apply adequate haircuts to collateral asset values that take into account the liquidity risk following the default of a market participant and concentration risk, and that reflect the potential for the value of such assets to decline over the interval between their last reevaluation and the time by which they reasonably can be assumed to be liquidated. Such haircuts shall consider, for each among other factors, the type of asset and the credit risk associated with the financial instrument, the maturity of the asset; the historical and hypothetical future price volatility of the asset in stressed market conditions; the liquidity of the underlying market,

including bid/ask spread; the foreign exchange risks; and any wrong-way risk. The CCP shall test its haircuts at least monthly.

Commission Determination: The Commission finds that the provisions of the EMIR Framework with respect to risk management are generally similar to Core Principle D and CFTC regulation 39.13, and prescribe how CCPs should monitor, evaluate, and manage the risks to which they are exposed. These standards seek to ensure that CCPs can meet their financial obligations to market participants, thus contributing to the financial integrity of the derivatives market as a whole.

Both regimes include a broad, general requirement for a DCO/CCP to manage the risk to which it is exposed and both regimes require the appointment of a CRO to perform similar functions. Both regimes require a DCO/CCP to use risk control mechanisms, such as margin requirements, to limit exposure to potential clearing member defaults. Similarly, both regimes require that margin models and parameters be risk-based and regularly reviewed and both regimes require that the calculation of initial margin include factoring the risk characteristics of each cleared product. Both regimes require at least a 99% confidence level in determining the adequacy of initial margin and both regimes have similar proscriptions for back testing initial margin models. Finally, both regimes require that cash balances must be either invested or appropriately safeguarded in a manner that bears little or no principal risk.

Accordingly, the Commission finds that the provisions of the EMIR Framework with respect to risk management standards discussed above and identified below in Table 1(b) are comparable to and as comprehensive as the risk management requirements of CFTC regulation 39.13, with the exception of 39.13(g)(8)(i) and (ii), which respectively

require FCMs to calculate initial margin for cleared customer accounts on a gross (as opposed to net) basis and require DCOs to collect additional initial margin for non-hedge positions of FCM customers. Despite the importance of gross margining of customer accounts and the collection of this additional initial margin, in an effort to promote comity, the Commission would not require DCO/CCPs to apply either of these regulations to non-FCM clearing member intermediaries or to the customers of non-FCM clearing member intermediaries. Additionally, the Commission makes this finding notwithstanding that the EMIR Framework's treatment of affiliates does not shield customers from potential losses by affiliates of the clearing member in the same manner as the CFTC's approach and in fact potentially exposes customers to proprietary trading losses.

Table 1(b): Risk Management		
Subject Area	CFTC Regulations	EMIR Framework
General/documentation requirement	17 CFR 39.13(a)-(b)	RTS-CCP, Art 4
Chief risk officer	17 CFR 39.13(c)	RTS-CCP, Art 3(3) and 4(6)
Limitation of exposure to potential losses from defaults	17 CFR 39.13(f)	EMIR, Art 48(2)
Margin models/parameters	17 CFR 39.13(g)(1)	EMIR, Art 41(2), 49(1)
Risk factors for margin	17 CFR 39.13(g)(2)(i)	RTS-CCP, Art 24(2)(b)
Minimum confidence level	17 CFR 39.13(g)(2)(iii)	RTS-CCP, Art 24(1)
Lookback period	17 CFR 39.13(g)(2)(iv)	RTS-CCP, Art 25
Regular independent validation	17 CFR 39.13(g)(3)	RTS-CCP, Art 47 and 59(1)
Portfolio margining	17 CFR 39.13(g)(4)	RTS-CCP, Art 27; RTS-CCP, Art 59(9)
Margin Back tests	17 CFR 39.13(g)(7)	RTS-CCP, Art 49 and 60(2)

Daily valuation of collateral posted as initial margin	17 CFR 39.13(g)(11)	RTS-CCP, Art 40(2)
Haircuts	17 CFR 39.13(g)(12)	EMIR, Art 46(1); RTS-CCP, Art 41(2) and 59(10)
Daily determination of initial margin adequacy	17 CFR 39.13(g)(6)	EMIR, Art 49(1)

C. Settlement Procedures (Regulation 39.14)

CEA Section 7a-1(c)(2)(E) (“Core Principle E”) establishes general requirements for DCOs to have sufficient settlement procedures. To implement Core Principle E the Commission adopted regulation 39.14, which requires a DCO to complete money settlements on a timely basis, but not less frequently than once each business day; employ money settlement arrangements to eliminate or strictly limit exposure to settlement bank risks; maintain an accurate record of the flow of funds associated with money settlements; possess the ability to comply with the terms and conditions of any permitted netting or offset arrangement with another DCO; establish rules that clearly state the obligation of a DCO with respect to physical deliveries; and ensure that a DCO identifies and manages each risk arising from any of its obligation with respect to physical deliveries.

Commission Requirement: Regulation 39.14 requires that a DCO collect margin from its clearing members on a daily basis. Specifically, a DCO must effect settlement with each clearing member at least once each business day, and must have the authority and operational capacity to effect a settlement with each clearing member on an intraday basis, either routinely, when thresholds specified by the DCO are breached, or in times of extreme market volatility.⁴⁸

⁴⁸ 17 CFR 39.14(b).

CFTC regulation 39.14 provides that a DCO must employ settlement arrangements that eliminate or strictly limit its exposure to settlement bank risk, by among other things, having documented criteria with respect to those banks that are acceptable settlement banks for the DCO and its clearing members, including criteria addressing the capitalization, creditworthiness, access to liquidity, operational reliability, and regulation or supervision of such banks.⁴⁹ A DCO further must monitor each approved settlement bank on an ongoing basis to ensure that such bank continues to meet the DCO's established criteria.⁵⁰

A DCO must monitor the full range of and concentration of its exposure to its own and its clearing members' settlement bank(s) and assess its own and its clearing members' potential losses and liquidity in the event that the settlement bank with the largest share of settlement activity were to fail. A DCO must take any one or more of the following actions, as needed, to eliminate or strictly limit such exposures: maintain accounts at one or more additional settlement banks; approve one or more additional settlement banks that its clearing members could choose to use; impose concentration limits with respect to one or more of its own or its clearing members' settlement banks; and/or take any other appropriate actions.⁵¹

A DCO must maintain an accurate record of the flow of funds associated with each settlement.⁵²

A DCO must possess the ability to comply with each term and condition of any permitted netting or offset arrangement with any other clearing organization.⁵³

⁴⁹ 17 CFR 39.14(c)(1).

⁵⁰ 17 CFR 39.14(c)(2).

⁵¹ 17 CFR 39.14(c)(3).

⁵² 17 CFR 39.14(e).

For products that are settled by physical transfer of the underlying instruments or commodities, a DCO must establish rules that clearly state each obligation that the DCO has assumed with respect to such physical deliveries, including whether it has an obligation to make or receive delivery of a physical instrument or commodity, or whether it indemnifies clearing members for losses incurred in the delivery process, and ensure that the risks of each such obligation are identified and properly managed.⁵⁴

Regulatory Objective: On a daily basis, DCOs are exposed to significant inflows and outflows of cash and other liquid financial instruments. Core Principle E and the Commission's implementing regulations are designed to ensure that a DCO has the authority and operational capacity to effect settlement with each clearing member, on an intraday basis and to also monitor, eliminate, or strictly limit the settlement risks to which a DCO is exposed.

Comparable EU Law and Regulations: The following provisions of the EMIR Framework address settlement procedures.

EMIR, Art. 41(1) and (3): A CCP shall impose, call, and collect margins to limit its exposures from its clearing members, and where relevant, from CCPs with which it has interoperability arrangements. Such margins shall be sufficient to cover potential exposures that the CCP estimates will occur until the liquidation of the relevant positions. Such margins also shall be sufficient to cover losses that result from at least 99% of the exposures' movements over an appropriate time horizon and they shall ensure that a CCP fully collateralizes its exposures with all its clearing members, and, where relevant, with CCPs with which it has interoperability arrangements, at least on a daily basis. A CCP

⁵³ 17 CFR 39.14(f).

⁵⁴ 17 CFR 39.14(g).

shall regularly monitor and, if necessary, revise its margins to reflect current market conditions, taking into account any potential procyclical effects of such revisions. A CCP shall call and collect margins on an intraday basis, at a minimum when predefined thresholds are exceeded.

EMIR, Art. 50(1): Where practical and available, a CCP shall use central bank money to settle its transactions. Where a CCP cannot use central bank money, it shall take steps to strictly limit cash settlement risk.

RTS-CCP, Art. 4(2), 32(4)(a), and 51(3): A CCP shall take an integrated and comprehensive view of all relevant risk, including the risks it bears from and poses to, among other things, settlement banks. A CCP also shall assess the liquidity risk it faces, including situations in which the CCP or its clearing members cannot settle their payment obligations when due as part of the clearing or settlement process. Such assessment shall address the liquidity needs arising from the CCP's relationship with, among others, settlement banks. As part of its stress testing procedures, a CCP should consider stress testing scenarios involving the technical or financial failure of, among others, its settlement banks.

RTS-CCP, Art. 13 and Art. 14(3): A CCP shall maintain records of all transactions in all contracts it clears and shall ensure that its records include all information necessary to conduct a comprehensive and accurate reconstruction of the clearing process. A CCP shall make, and keep updated, a record of the amounts of margin, default fund contributions, and other financial resources, with respect to each single clearing member and client account, if known to the CCP.

EMIR, Art. 50(2)-(3): A CCP shall clearly state its obligations with respect to deliveries of financial instruments, including whether it has any obligation to make or receive delivery of a financial instrument or whether it indemnifies participants for losses incurred in the delivery process. Where a CCP has an obligation to make or receive deliveries of financial instruments, it shall eliminate principal risk by using delivery-versus-payment mechanisms, to the extent possible.

Commission Determination: The Commission finds that the provisions of the EMIR Framework with respect to settlement procedures are generally similar to Core Principle E and CFTC regulation 39.14, and eliminate or strictly limit a CCP's exposure to settlement risk. Both regimes require the daily collection of margin and both require a DCO/CCP to employ settlement arrangements that limit exposure to various risks, including exposure to settlement banks, concentration risk, and physical delivery of instruments. Both regimes have similar recordkeeping requirements. Finally, both regimes require a DCO/CCP to have rules with respect to the physical delivery of an instrument or commodity, and to identify and manage the risks associated with the physical delivery of such instruments.

Accordingly, the Commission finds that the provisions of the EMIR Framework with respect to settlement procedures discussed above and identified below in Table 1(c) are comparable to and as comprehensive as the default rules and procedures of CFTC regulation 39.14.

For the avoidance of doubt, the Commission notes that the foregoing comparability determination only applies with regard to certain provisions of regulation 39.14 (i.e., § 39.14(b), § 39.14(c), § 39.14(e), § 39.14(f), and § 39.14(g)). No

comparability finding is made regarding § 39.14(d), which requires a DCO to ensure that settlements are final when effected by ensuring that it has entered into legal agreements that state that settlement fund transfers are irrevocable and unconditional no later than when the DCO's accounts are debited or credited.

Table 1(c): Settlement Procedures		
Subject Area	CFTC Regulations	EMIR Framework
Settlement procedures	17 CFR 39.14(b), (c), (e)-(g)	EMIR, Art. 41(1) and (3); EMIR, Art 50(1); RTS-CCP, Art 4(2), 32(4)(a) and 51(3); RTS-CCP, Art 13 and 14(3); EMIR, Art 50(2)-(3).

D. Default Rules and Procedures (Regulation 39.16)

CEA Section 7a-1(c)(2)(G) (“Core Principle G”) establishes general requirements for DCOs to have adequate default rules and procedures. To implement Core Principle G the Commission adopted regulation 39.16, which requires a DCO to have rules and procedures designed to allow for the efficient, fair, and safe management of events during which members or participants become insolvent or otherwise default on the obligations of the members or participants to the DCO.

Commission Requirement: CFTC regulation 39.16 provides requirements by which a DCO must adopt rules and procedures designed to allow DCOs to effectively manage events during which clearing members become insolvent or default on the obligations of such clearing members to the DCO.⁵⁵

Pursuant to CFTC regulation 39.16, a DCO must adopt procedures that would permit the DCO to timely take action to contain losses and liquidity pressures and to continue meeting its obligations in the event of a default on the obligations of a clearing

⁵⁵ 17 CFR 39.16(a).

member to the DCO.⁵⁶ Further, a DCO must adopt rules setting forth its default procedures; including the DCO's definition of default, the actions that the DCO may take upon default, which must include the prompt transfer, liquidation, or hedging of the customer or house positions of the defaulting clearing member, as applicable, and which may include, in the DCO's discretion, the auctioning or allocation of positions to other clearing members; any obligations that the DCO imposes on its clearing members to participate in auctions or to accept allocations, of the customer or house positions of a defaulting clearing member, subject to certain limitations; the default waterfall – i.e., the sequence in which the funds and assets of the defaulting clearing member and its customers and the financial resources maintained by the DCO would be applied in the event of a default; and a provision that the funds and assets of a defaulting clearing member must be applied to cover losses with respect to a customer default, if the relevant customer funds and assets are insufficient to cover the shortfall.⁵⁷ The DCO must make its default rules publicly available.⁵⁸

Regulatory Objective: Core Principle G and the Commission's implementing regulations are designed to ensure that each DCO clearly states its default procedures, makes its default rules publicly available, and has rules and procedures that allow it to take timely action to contain losses and liquidity pressures and to continue meeting its obligations.

Comparable EU Law and Regulations: The following provisions of the EMIR Framework address default rules and procedures.

⁵⁶ 17 CFR 39.16(c)(1).

⁵⁷ 17 CFR 39.16(c)(2)(i)-(v).

⁵⁸ 17 CFR 39.16(c)(3).

EMIR, Art. 48: A CCP shall have written procedures to be followed in the event of the default of a clearing member. The CCP shall take prompt action to contain losses and liquidity pressures resulting from defaults and shall ensure that the closing out of any clearing member's positions does not disrupt its operations or expose the non-defaulting clearing members to losses that they cannot anticipate or control.

EMIR, Art. 37(6): A CCP may impose specific additional obligations on clearing members, including the participation in auctions of a defaulting member's positions. Such obligations shall be proportional to the risk brought by the clearing member and shall not restrict participation to certain categories of clearing members.

EMIR, Art. 45: A CCP shall use a defaulting clearing member's margins before using other financial resources to cover losses. Where the margins posted by the defaulting clearing member are insufficient to cover the losses covered by the CCP, the CCP shall use the default fund contribution of the defaulting member to cover the loss. A CCP shall use contributions to the default fund of the non-defaulting clearing members and any other financial resources only after having exhausted the defaulting clearing member's contributions. A CCP further shall use its own dedicated financial resources before using the default fund contributions of non-defaulting clearing members. A CCP shall not use the margins posted by non-defaulting clearing members to cover losses resulting from the default of another clearing member.

RTS-CCP, Art. 58 and 59(12): At least on a quarterly basis, a CCP shall test and review its default procedures to ensure they are both practical and effective. At least annually, a CCP shall perform simulation exercises as part of the testing of its default

procedures. It also shall perform simulation exercises following any material change to its default procedures.

ESMA Q&A CCP Question 8(f)(1): A CCP shall use the margins posted by a defaulting clearing member prior to other financial resources when covering losses and may have rules which allow it to use surplus margin on a defaulted clearing member's house account to meet any obligation of the clearing member with respect to losses on a client account of that clearing member. For the avoidance of doubt, surplus margin on a client account of a default clearing member cannot be used to meet any losses on the defaulted clearing member's house account(s).⁵⁹

RTS-CCP, Art. 61(2): A CCP shall make publicly available key aspects of its default procedures, including the circumstances in which action may be taken, who may take action, the scope of the actions that may be taken (including the treatment of both proprietary and client positions, funds and assets), and the mechanisms for addressing a CCP's obligations to non-defaulting clearing members.

Commission Determination: The Commission finds that the provisions of the EMIR Framework with respect to default rules and procedures are generally similar to CFTC regulation 39.16, and prescribe how CCPs should clearly state their default procedures. Both regimes require a DCO/CCP to have detailed procedures to follow in the event of a default, including requirements for the orderly transfer and/or liquidation of customer or proprietary positions, participation in auctions, the sequence of the default waterfall, and public disclosure of the default procedures. These standards seek to ensure

⁵⁹ Questions and Answers: Implementation of the Regulation (EU) No 648/2012 on OTC derivatives, central counterparties and trade repositories (EMIR)
https://www.esma.europa.eu/system/files_force/library/2016-293_qa_xvi_on_emir_implementation.pdf?download=1.

that CCPs may take timely action to contain losses and liquidity pressures and to continue meeting their obligations.

Accordingly, the Commission finds that the EMIR Framework with respect to default rules and procedures discussed above and identified below in Table 1(d) are comparable to and as comprehensive as the default rules and procedures of CFTC regulation 39.16.

For the avoidance of doubt, the Commission notes that the foregoing comparability determination only applies with regard to the above mentioned provisions of CFTC regulation 39.16 (i.e., § 39.16(a), § 39.16(c)(1), § 39.16(c)(2)(i)-(v), and § 39.16(c)(3)). No comparability finding is made regarding the other provisions of § 39.16, namely § 39.16(b), which requires a DCO to maintain a written default management plan, and § 39.16(d), which requires a DCO to have certain rules in place regarding the insolvency of clearing members.

Table 1(d): Default Rules and Procedures		
Subject Area	CFTC Regulations	EMIR Framework
Default rules & procedures	17 CFR 39.16(a), 17 CFR 39.16(c)(1) 17 CFR 39.16(c)(2)(i)-(v) 17 CFR 39.16(c)(3)	EMIR, Art 48, 37(6) and 45; RTS-CCP, Art 58, 59(12) and 61(2); ESMA Q&A CCP Question 8(f)1.

VI. DCO/CCP Registration

Section 5b(a) of the CEA and Commission Regulations 39.1 and 39.3 require a DCO to register with the Commission in the format and manner specified by the Commission. In particular, Regulation 39.3 specifies that a DCO seeking registration from the Commission must file a Form DCO and various supporting exhibits.

In the interest of comity, the Commission generally will tailor its registration process both in terms of administration and substantive review to reflect the availability of substituted compliance for EU CCPs. Accordingly, consistent with Regulation 39.3, EU CCPs seeking registration must complete Form DCO. However, with respect to questions and information requirements in areas where compliance with the EMIR Framework is substituted for compliance with part 39, the EU CCP may evidence its compliance with the EMIR Framework in lieu of its compliance with part 39. DCO/CCPs that are already dually registered need not take any further action to take advantage of the substituted compliance determinations made under this Notice. These determinations will be applied automatically to all current DCO/CCPs registrants.

Moreover, to streamline the registration process, an EU CCP applicant may, instead of submitting the exhibits required under the CFTC Form DCO regulation, use existing materials that it has submitted to its NCA for its EMIR authorization or other relevant documents produced by its NCA that demonstrate compliance with EMIR provisions for which substituted compliance is available (e.g., supervisory examination reports or reports from its NCA). The positive opinion of the CCP supervisory college should also be submitted to the Commission by way of supporting evidence. The Commission will not require an EU CCP to obtain certification from its NCA, certifying that it has complied with the EMIR Framework.

In addition, for the Form DCO documents listed below, the Commission will accept a copy of the original document filed by the EU CCP with its NCA with an attestation by that authority that they are acceptable to that authority:

- Exhibit A-8: articles of incorporation or similar corporate documents;

- Exhibit A-10: outside service provider agreements;
- Exhibit E-1(4): settlement bank agreements;
- Exhibit F(a)(2): depository agreements; and
- Exhibit M(a): information-sharing agreements.

If these documents are not in English, and an English translation is available, the EU CCP applying for registration should provide the English translation. If an English translation is not available, the EU CCP applying for registration should inform the Commission in writing but need not provide a translated version unless requested by the CFTC.

The Commission will review the documentation received to determine if it is complete and comprehensive. In the case that information evidencing compliance with the EMIR Framework is incomplete, the Commission will seek to obtain further evidence from the relevant NCA evidencing its assessment of compliance. If the documentation is still not sufficient for the Commission to review compliance with the terms of the EMIR Framework, the Commission will request additional evidence from the CCP and notify the NCA of the request made.

The Commission will seek to obtain any other missing information from the relevant EU CCP. The Commission also will provide the relevant NCA with the opportunity to be consulted with respect to any questions if so requested at the outset by that authority.

VII. Limited Application of Certain CFTC Regulations

As a general matter, the Commission acknowledges that CCPs registered in foreign jurisdictions operate under different regulatory regimes, and that the differences

between these various regimes may lead to regulatory arbitrage. The Commission also understands that the CFTC staff intends to provide limited no-action relief for DCO/CCPs from the application of Commission regulations to discrete aspects of a DCO/CCP's non-U.S. clearing activities as set forth below when this Notice becomes effective.

(1) CFTC Regulation 39.12(b)(6)'s requirement that, upon a DCO's acceptance of a swap for clearing, the original swap is extinguished and it is replaced by an equal and opposite swap between the DCO and each clearing member acting as a principal for a house trade or an agent for a customer trade will not apply where neither party is a U.S. clearing member or an FCM clearing member;

(2) Part 22 of CFTC Regulations and its "legally segregated but operationally commingled" ("LSOC") account model for cleared swaps customer accounts will not apply to clearing members that are not FCMs;

(3) CFTC Regulation 39.13(g)(8)(i)'s requirement that initial margin for customer accounts cleared by an FCM be calculated and collected on a gross basis would not apply to non-FCM clearing member intermediaries;

(4) CFTC Regulation 39.13(g)(8)(ii)'s requirement that a DCO collect initial margin at a level that is greater than 100% of the DCO's initial margin requirements for the non-hedge positions of FCM customers will not apply to non-FCM clearing member intermediaries;

(5) CFTC Regulation 39.12(a)(2)(iii)'s prohibition that a DCO not set a minimum capital requirement of more than \$50 million for any person that seeks to become a

clearing member to clear swaps will not apply to non-U.S. clearing members or non-FCM clearing members;

(6) CFTC Regulation 39.12(b)(7)'s requirement that DCOs utilize "straight-through-processing" of swaps submitted for clearing will not apply to trades that are not executed on or subject to the rules of a DCM or a swap execution facility and for which neither clearing member is an FCM, a swap dealer, or a major swap participant;

(7) Regulation 39.13(h)(5)'s requirement that DCOs must require their clearing members to maintain written risk management policies and procedures and that DCOs must have the authority to obtain information and documents from clearing members regarding their risk will still apply; however, DCO/CCPs may implement different oversight programs for U.S./FCM clearing members and non-U.S. clearing members; and

(8) Regulation 39.11(f)'s and Regulation 39.19(c)(3)(ii)'s implicit requirements that DCOs submit to the CFTC quarterly financial resource reports and an audited year-end financial statement that are prepared in accordance with GAAP will not apply; rather, the DCO/CCPs may submit financial statements prepared in accordance with IFRS, with periodic reconciliation to assist staff in reviewing the financial statements.

VIII. Supervisory Arrangement

As noted above, with respect to dually-registered DCO/CCPs, the Commission retains its examination authority with respect to DCO/CCPs and requires that home country regulator(s) enter into an MOU that addresses how the regulator(s) will cooperate and share information with respect to supervision of the DCO/CCP. Thus, the Commission has entered into a supervisory MOU with the home country regulator(s) of a

DCO/CCP.⁶⁰ For dual registrants in the future, the Commission similarly expects that an MOU will establish procedures for ongoing cooperation, address direct access to information, provide for notification upon the occurrence of specified events, memorialize understandings related to on-site visits, and include protections related to the use and confidentiality of non-public information shared pursuant to the MOU.

While certain principles of supervision are universal, based on its experience supervising DCO/CCPs, the Commission recognizes the benefits of tailoring a joint supervisory regime to (1) the unique legal and regulatory framework in which each regulator operates and (2) the unique financial, operational, and organizational characteristics of each DCO/CCP. With respect to CFTC regulations for which there would be substituted compliance, the Commission generally believes that there should be joint examinations. By way of example, Commission staff already has participated in joint examinations with the Bank of England, and the Commission believes that joint examinations can be an efficient means for effective, in-depth review of a DCO/CCP's regulatory compliance.

However, depending on the individual circumstances, it may be appropriate for the home country regulator(s) to assume greater responsibility for conducting the examinations. The Commission expects that its staff would be flexible in determining their approach to a given examination based on the nature and scope of the examination. Therefore, with the overall goal of applying uniform principles in a consistent yet flexible way, the Commission intends to address supervisory matters, including examinations, on

⁶⁰ The Commission also requires an MOU with respect to exempt DCOs.

a case-by-case basis for each individual DCO/CCP in close consultation with the relevant home country regulator(s).

IX. Conclusion

As noted above, the Commission finds that each provision of the EMIR Framework discussed above, is comparable to and comprehensive as the Commission requirements identified above and thus a CCP's compliance with the identified provisions of the EMIR Framework will satisfy compliance with the corresponding Commission requirements.

Issued in Washington, DC, on March 16, 2016, by the Commission.

Christopher J. Kirkpatrick,
Secretary of the Commission.

Appendices to Comparability Determination for the European Union: Dually-Registered Derivatives Clearing Organizations and Central Counterparties – Commission Voting Summary, Chairman's Statement, and Commissioner's Statement

Appendix 1 – Commission Voting Summary

On this matter, Chairman Massad and Commissioners Bowen and Giancarlo voted in the affirmative. No Commissioner voted in the negative.

Appendix 2 – Statement of Chairman Timothy G. Massad

Today, the CFTC has taken action to implement our agreement with the European Commission regarding requirements for central clearing counterparties (CCPs). Our unanimous action today means that European CCPs registered with the CFTC can comply with many of our rules by meeting the corresponding European Market Infrastructure Regulation (EMIR) requirements.

The equivalence agreement announced by European Commissioner Jonathan Hill and myself is an important step in achieving cross-border harmonization of derivatives regulation. It provides a foundation for cooperation among regulators in the oversight of the global clearinghouses that are so important in our financial system today. It resolves the issues that were standing in the way of Europe recognizing U.S. CCPs. And it helps make sure that the U.S. and European derivatives markets can continue to be dynamic, with robust competition and liquidity across borders.

The action we have taken today is an important component of that agreement. The notice identifies the rules for which the CFTC will grant substituted compliance. These include rules related to CCP financial resources, risk management, settlement procedures, and default management. We have also streamlined the process for registration, which will further harmonize our regimes.

Finally, CFTC staff today are also providing no-action relief from the application of Commission regulations to discrete aspects of a clearinghouse's non-U.S. clearing activities.

The Commission is working with U.S. clearinghouses seeking recognition by the European Securities and Market Authority (ESMA) to ensure ESMA has all necessary

information to review their applications in a timely manner. I look forward to ESMA completing the recognition process in a manner that ensures the global derivatives markets can continue to function efficiently and without disruption.

Appendix 3 – Statement of Commissioner J. Christopher Giancarlo

I support the comparability determinations issued by the Commodity Futures Trading Commission (“CFTC”).

Today’s action furthers the commitment to a common approach for transatlantic central clearing counterparties (CCPs) announced on February 10, 2016 by my colleague, CFTC Chairman Timothy Massad, and Commissioner Jonathan Hill of the European Commission (EC). Under the comparability determinations, CCPs that are authorized in the European Union (EU) under the European Market Infrastructure Regulation (EMIR) and registered with the CFTC may comply with certain CFTC requirements for financial resources, risk management, settlement procedures, and default rules and procedures by complying with corresponding requirements under the EMIR framework. Today’s notice also provides for a streamlined approach for EU CCPs that may wish to register with the CFTC in the future.

As I said when it was announced, the agreement reached between the EC and the CFTC avoids unacceptable changes to four decades of U.S. clearinghouse margin policy and higher costs of hedging risk for America’s farmers, ranchers, financial institutions, energy firms and manufacturers.

Yet, as I have observed, the protracted process for reaching this compromise was made needlessly complex because both the EC and the CFTC insisted on a line-by-line rule analysis contrary to the flexible, outcomes-based approach advocated by the OTC

Derivatives Regulators Group. While the end result is a good one, the approach taken to get here was needlessly circuitous and uncertain.

The CFTC and its global counterparts must now recommit themselves to work together to implement an equivalence and substituted compliance process, particularly for swaps execution and the cross-border activities of swap dealers and major swaps participants, based on common principles in order to increase regulatory harmonization and reduce market balkanization.¹ The future of the global swaps marketplace depends on it.

¹ See, e.g., IOSCO Task Force on Cross-Border Regulation, Final Report (Sept. 2015) (advocating for an outcomes-based approach as opposed to a line-by-line comparison of rules).

